

Budgetary and accounting experience in public sector- comparative case study

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During the last decade the public sector has been affected by the introduction of significant reforms in the public accounting system in the international context.

During the reform process different countries have put into practice numerous intermediate variants between the extremes of cash and accrual budgeting and accounting. The reasons for the different national systems may be due to the culture, the historical background or the structural elements of these countries. Also the specific objectives and the principal users of the financial reporting, the financial resource suppliers and the influence of public accounting regulatory bodies imply different national accounting systems.

In the Western democracies there are two main broad styles of public management: Anglo-American and European Continental types.

The paper presents the United Kingdom accrual accounting model adopted in the public institutions (an Anglo-Saxon country) by comparison with the Romanian one (a Continental European country). In this paper there will be taken into account some case studies of two public institutions: one from United Kingdom and the other from Romania.

The paper tries to emphasize the differences and the similarities between the two countries accounting systems as well as the lessons learned from the United Kingdom accounting system regarding the implementation of the accrual accounting in public sector.

Keywords: accrual accounting, public public sector, the United Kingdom, Romania, International Public Sector Accounting Standards.

1 Introduction

The public sector is more and more affected by significant reforms in the public accounting system in the international context. The aim of the public sector reforms is to overcome bureaucratic obstacles so that managers can use their limited resources more efficiently (Pina, V. and Torres, L., 2003). Accounting played a crucial role in the public management development once the autonomy in public service organizations increased.

The use of the cash or accrual basis of budgeting and accounting was seen as a great divide between the public and private sector with the public sector practicing cash accounting and budgeting, and the private sector using accrual methods. The better the financial information, the increase in the cost transparency and the valuation of public sector assets (Graham A., 2005) have persuaded many countries to adopt the accountancy system to their own needs. During the reform process they have put into practice numerous intermediate variants between the extremes of cash and accrual budgeting and accounting. The reasons for the different national systems may be due to the culture, the historical background or the structural elements of these countries. Also the specific objectives and the principal users of the financial reporting, the financial resource suppliers and the influence of public accounting regulatory bodies imply different national accounting systems.

In the Western democracies there are two main broad styles of public management: Anglo-American and European Continental types. Anglo-American countries (Australia, Canada, New Zealand, United Kingdom and the United States) have undertaken territorial decentralization and have adapted the private sector experience to the public sector. They are more likely to introduce market mechanisms and notions of competitiveness and envisage the citizen primarily as a consumer of services or as a client (Pina, Torres, 2003). The European Continental countries (Belgium, France, Germany, Greece, Portugal, Romania and Spain) are influenced by structures inherited from a bureaucratic and hierarchical public administration, grounded in administrative law (Pina, Torres, 2003).

Although there is a wide acceptance of the application of the accrual systems for the production of accounting statements, there is no consensus with regard to the production of the budgetary statements. The tendency of most countries is to produce budgets according to the accrual criterion, producing a forecast statement of revenues and expenses, cash flows and the financial situation (Brusca and Condor, 2002). European Union member countries are required to

prepare government forecast and financial statements in accordance with the European System of Accounts (ESA 95) ¹ (Athukorala and Reid, 2003). It appears that all the European countries have adapted or are intending to adopt ESA 95. In the European Union the free circulation of information is essential. An important item is the converging and the harmonization between the public accounting system in different countries.

The use of alternative criteria in public accounting systems leads to different results concerning the financial statements, the income and expenditure statements and the balance sheet. In spite of these, public accounting harmonization is taking its first steps through the efforts of INTOSAI (International Organization of Supreme Audit Institutions) and IFAC (International Federation of Accountants) at global level.

The standards of INTOSAI have mainly focused on the elaboration of a conceptual framework for public accounting information. The IFAC standards entered into more detailed recommendations on accounting practices adapting the International Accounting Standards for public entities under the influence of the Anglo-Saxon Model and passing over the importance of the budget from the Continental European Model or of the features of public sector accounting (Brusca and Condor, 2002). Although some international organizations (OCDE and European Union Institutions) have adapted the International Public Sector Accounting Standards (IPSAS), different countries, especially from the Continental European area, are not very interested in adopting them because of the difference to the continental accounting tradition (Brusca and Condor, 2002).

This paper presents the United Kingdom accrual accounting model adopted in the public sector (an Anglo-Saxon country) by comparison with the Romanian one (a Continental European country) trying to emphasize the differences and the similarities between the two countries accounting systems as well as the lessons learned from the United Kingdom accounting system regarding the implementation of the accrual accounting in public sector. In this paper we undertake some brief comparisons concerning the budgeting and the accounting practices in the public sector between the United Kingdom system and the Romanian one. The main aspects to which we refer are the budgetary system and the role of the budget in public institutions, the types of financial statements produced and the accounting conventions regarding the valuation and the accounting registration.

2 Comparisons regarding the budgetary system between the United Kingdom and Romania

2.1 The financial control system

One of the differences between the Romanian and the United Kingdom system is the financial control system. The focus of control in the Romanian system is to ensure that cash expended in the period (or income collected) is neither greater nor less than forecasts in the budget. The emphasis is therefore about “inputs” into the activity rather than what the activity achieved (outputs). The main forms of Romanian higher education institutions management control is on “time”, e.g. when an invoice is to be paid, and it is possible for the manager to manipulate timing in order to ensure that budgets are met. In the United Kingdom system this is considerably less possible and managers have no ability to influence time. They are focused on resources used and the price paid for those resources.

2.2 The purpose of the budgetary system and its link to the accounting system

In Romanian public institutions the purpose of the budgetary appropriations registration is to provide information at every stage and for every subdivision of the approved budget concerning the consumed budgetary credits. For this reason, at every level, credit holders who are responsible for the accountancy organization and the book-keeping are designated according to the legal stipulations.

The commitments and payments are controlled on the basis of the authorisation of the Parliament. The cash deficit is directly linked to the appropriations. For this reason there is set a budgetary execution system through a budgetary accounting method which records the budgetary expenditures with a single-entry book-keeping procedure through some accounts which are not included in the balance-sheet, like “Budgetary Approved Credits”, “Budgetary Commitments”. These accounts record on their debit the opening balance at the beginning of the year, and every entry during the year, of the credits and commitments and on their credit the exits during the year and the close at the end of the year. While the Romanian budgetary system can be exercised at a detailed level registering and controlling the income and expenditure without providing managerial information, the resource budgeting system applied in the United Kingdom public institutions permits the control over the cash spending at a less detailed level and the relevance of the information permits the United Kingdom institutions managers a more soundly based control of expenditure.

Also, the resource budgeting approach requires higher education departments to consider the cost of capital consumption and to match their costs to the time of the related service delivery activity (Economic&Social Research Council, 2005). Departmental budgets also include charges for depreciation on their assets (HM Treasury, 2005). The focus on resources rather than cash consumption reflects the economic significance of capital and current expenditure and encourages greater emphasis on outputs and on the achievement of aims and objectives (Mellet, 1998).

3 Comparisons regarding public entities accounting system between the United Kingdom and Romania

The Romanian accounting system has a strong orientation marked by the macro-economical information needs, the United Kingdom accounting tries to satisfy both government departments and agencies and other groups of users like employees, suppliers, students, other customers, lenders, general public. As both the Romanian and the United Kingdom public accounting systems have the accrual accounting at their basis, between the two systems there are not too many structure differences. The differences start from the economical politics as well as from the political and constitutional influences. The comparisons regarding the public higher education institutions between the United Kingdom and Romania have as a main objective:

- Characteristic elements;
- Financial statements;
- Valuation and accountability registration.

3.1 The characteristic elements of the public higher education institutions accounting

The main elements which characterize the two accounting systems from the public higher education institutions are shown in the Table no. 1.

Elements	The characteristics of the public institutions accounting from the United Kingdom	The characteristics of the public institutions accounting from Romania
Basis of the accounting system	Accrual accounting organized in a double-entry system, with no use of a numbered chart of accounts.	Accrual accounting organized in a double-entry system, with the use of a numbered chart of accounts.
Accounting organization	The accounting is organized into a fiscal year.	The accounting is organized into a financial year which is identical with the calendar year.
Accounting regulations	The adopting of the General Accepted Accounting Standards of the United Kingdom, without taking into account the International Public Sector Accounting Standards (IPSAS).	Most of the legislative regulations are made by the Ministry of Public Finance, taking into account the International Public Sector Accounting Standards (IPSAS).
Institutional differences	The Treasury has no role in the administration of the public higher education institutions liquidity, being a part of the governmental body. The liquidity administration is done by the central and commercial banks.	The Treasury plays an important role, being responsible for the liquidity administration of the public higher education institutions.
Sectored accounting	There is a sectored accounting plan in two accounting cycles, each functioning autonomously but in parallel with the others: <ul style="list-style-type: none"> ▪ financial accounting, ▪ cost and management accounting. 	There is a sectored accounting plan in three accounting cycles, each functioning autonomously but in parallel with the others: <ul style="list-style-type: none"> ▪ financial accounting, ▪ cost and management accounting, and ▪ budget accounting.

Table 1
Comparisons regarding the main elements characteristically to the public institutions from the
United Kingdom and Romania

3.2 The financial statements worked out by the public entities

Comparing the accounting systems applied by the public entities from the two analyzed countries I observed the existence of some different treatments regarding the regularity of the financial reports. In the case of Romanian public universities the reporting of the financial statements are quarterly while in the case of the United Kingdom system these reports are half-yearly.

The main financial statements worked out by the public higher education institutions are as follows:

- balance sheet;
- income and expenditure account (outcome account);
- cash flow statement.

Table no. 2 shows the main financial statements as well as the financial statements required by the IPSAS 1 – “Presentation of Financial Statements”.

The main financial statements of the public entities from the United Kingdom	The main financial statements of the public entities from Romania	The main financial statements required by the IPSAS
1. Balance Sheet	1. Balance Sheet	1. Statement of Financial Position
2. Income and Expenditure Account	2. Patrimonial Outcome Account	2. Statement of Financial Performance
3. Cash Flow Statements	3. Treasury Flow Statements	3. Cash Flow Statements
4. Statement of Historic Cost Surpluses and Deficits	4. Statement of Changes in Net Assets/ Equity	4. Statement of Changes in Net Assets/ Equity
5. Notes to the Accounts	5. Appendixes to the Financial statements, Explanatory Notes	5. Accounting Policies and Notes to the Financial Statements
6. Statement of Total Recognised Gains and Losses	6. Budgetary Execution Account	
7. Governors' Report		

Table 2

The main financial statements of the public entities from the United Kingdom and Romania in comparison with the financial statements required by IPSAS 1

Although the shown components in the Table no.2. present different names, the “Statement of Financial Position” being called “Balance sheet”, the “Statement of Financial Performance” being called “Income and Expenditure Account” or “Patrimonial Outcome Account”, all of these represents the same thing, having as objective “the providing of information useful to the decision-making process and the demonstration of the entity responsibility for the committed resources” (IPSAS1). Another aspect which differentiates the financial statements of the two compared public entities is the presence of the Budgetary Execution Account in the Romanian public entities financial statements. The Budgetary Execution Account links the financial statements to the budgetary statements.

The different valuation mode of assets and liabilities and the different structure of the financial statements lead to different results.

Comparing the two countries, it is obvious that the use of financial statements can be divided between stewardship purposes and performance evaluation purposes (Rutherford *et al.*, 1992). The stewardship purpose is very well distinguished in the Romanian system because of the management of resources in the way originally intended, the public entities being able to meet their continuing obligations. By contrast, the United Kingdom system tries to follow the performance evaluation purposes, encompassing the idea of “how well” the higher education institutions obtains high quality and efficiency using the resources at their disposal. The United Kingdom accounting system regards a more private point of view and its scope is the providing of information for the management and for the general public. The financial statements emerging from the resource accounts are based on the standard commercial model of profit and loss account and balance sheet. However, the resource account formats differ from company formats in a number of respects to reflect the context and nature of every public institution. The Romanian system, because of the “cameralistic point of view” (Christiaens and deWielemaker, 2003), tends to register and to control the public expenses. The second significant Romanian financial statement is the Budgetary Execution Account that represents the fulfilment of the institution’s forecasts.

3.3 The valuation and the recognition of public entities assets and liabilities

The public entities have some specific characteristics which are distinguished through the way in which they are valued in the balance sheet: art galleries, museums and historical exhibits. These kinds of assets having only a cultural, social, artistic and historical background are actually not real business assets (Christiaens, de Wielemaker, 2003).

Both in Romania and in United Kingdom heritage buildings are maintained in such a state that their residual values are not materially different from their book values and hence a nil depreciation charge is made. Also, land is not depreciated. Both in Romania and in United Kingdom equipment is stated at cost and is depreciated. Both in Romania and in United Kingdom stocks are stated at the lower of cost and net realisable value. The different valuation mode leads to different results of the financial statements. Depreciation plays also an important role in establishing the real value of the assets.

For the Romanian public entities the ordering of an article involves the commitment of funds for cash forecasting purposes. Such commitments are “off balance sheet” and are recorded in a special account named “Budgetary Commitments” because it represents an encumbrance of funds and restricts their

alternative use, they are not recorded in the cash accounting system because they do not involve a formal transaction.

An important point of United Kingdom public entities is that the non-recurrent grants received for the acquisition or construction of fixed assets are treated as capital grants and amortised in line with depreciation over the life of the assets, while the Romanian universities grants, stated for basic and complementary activity, and are not depreciated.

The Romanian public accounting system works after a distinct chart of accounts used by all the public institutions and it particularly has some specific public entities accounts used for registering of entity incomes, expenditures and deductions. The United Kingdom accounting system doesn't use any chart of accounts, but entities have an advanced informatics system that helps the efficiency of the system usage.

Although between the two countries there are numerous differences both concerning the budget and accounting, the Romanian system has a solid informational base from which it can start the improvement of the budgeting and the accounting system. The comparisons have in view the identification of the weak points of the Romanian public system and the emphasis of an eloquent example for the Romanian entities taking into account the practical application of the accrual budgeting and accounting in United Kingdom entities and the advantages which arise from this system.

4 Lessons from the United Kingdom experience

The experience of the accrual accounting and budgeting in the United Kingdom proves that the system works transparently and it points to a good direction. All these advantages require some sacrifices. In the following rows I point out some lessons which the Romanian public system should take into account from the United Kingdom experience.

1. - The transition needs time The introduction of resource accounting and budgeting in the whole United Kingdom public accounting sector is not complete yet, the technical change was achieved but it is too early to say whether or not the change is successful. The transition to the resource (accrual) accounting and budgeting takes time. In the United Kingdom public system the period taken for implementation was about five years and more generally four in practice, starting with the local government sector and finishing with the central government.

2. - Accrual accounting and budgeting must be integrated Accrual accounting and budgeting should go together. The same basis of accounting and budgeting would provide a better management and financial control because the

information about previous years' activities remains, for most operations, the basis of future budgets.

3. – The tendency of developing entrepreneurial activities The enhancing of the services provided and the limited resources allocated to public entities lead to institution reorganisation, stimulating more and more the public entities to an entrepreneurial activity. The whole public sector is affected by a structure change, adopting the private sector techniques.

4. – Outputs over inputs, performance over control The methods of control and the distribution of responsibility should suffer significant changes in order to achieve the full benefits of accrual accounting and budgeting. The tendency is to control outputs rather than inputs providing managers with the opportunity to manage outputs having a relative freedom over inputs. In turn, managers should exercise a more rigorous discipline regarding the performance.

5. – The training of managers and responsible officials In order to implement the accrual accounting and budgeting, all the people implicated in the transitional process starting with the politicians, managers and responsible officials should understand the effective use of the system and accept the rules because of the complexity of the system. The cultural change requires investment in the training of managers and even the employees.

6. – The reorganisation of the arrangements In order to realise the benefits of accrual accounting and budgeting there are required some difficult decisions regarding closing or reorganising operations, removing staff, introducing competitive and regulatory arrangements.

7. – Information technology capability The implementation of accrual accounting and budgeting requires a more complex information technology (IT) system than those associated with the cash system in order to provide the information necessary for an efficient management of operations.

Resource accounting and budgeting is not the solution of the problems of the cash system, nor should accrual accounting be supported just because it is the current international fashion (OECD, 2002). The introduction of resource accounting and budgeting in the United Kingdom is a part of a long process of reform. All the signs are that in the United Kingdom the reform will be successful because of the structures and the will exists that will overcome all the difficulties. Our opinion is that the trend to the accrual accounting and budgeting is timely because the financial and managerial reorganisation of the public sector needs a new approach from the budgeting and accounting point of view. The approach tendency of the public system to the private system requires also the approach of the public budgeting and accounting system to the private one.

5 Conclusions

The economical development - marked by the market internationalization and by the enterprises activity, especially the growth of direct international investments - determine the nations to try more and more to draw together their accounting systems. The public accounting reform aims at transferring the private sector accounting and managerial principles and techniques to the public sector.

On the basis of these changes in the whole public sector, Romania, starting with 1st of January 2006, had to implement a new public accounting system able to face a more realistic reflection of the elements generated by all these transformations.

The transition poses more questions so, if the total renunciation to the cash accounting and budgeting seems simpler, the experience of other countries like United Kingdom shows that the step by step adoption of the accrual techniques is more convenient because the risk of the whole public financial system destabilization is not too big. The modification and the extensive role of the public sector accounting becomes obvious: instead of the out-of-date registration of the financial data and of the budget preparation, the United Kingdom accounting system has as a purpose the assets and the liabilities quantification and the improvement of the financial management performances. The accrual budgeting and accounting system has many advantages in improving decision-making process, proper control and management of public expenditure, entailing the use of performance indicators and the incorporation of department objectives in budgets.

There are a lot of opinions regarding the idea that the accrual accounting is inadequate from the point of view of the economical representation of a public institution. The decisive result according to cash accounting may lead to obvious errors when there is a gap between the sale-purchasing actions on the one hand, and the payments and receipts, on the other hand. The contemporary economy is very influenced by the credits. The phenomena generated by the credits are distinguished with the help of accrual accounting. The accrual accounting system is the only one which could provide information referring to the funds inputs and outputs in the monetary flows at the valuation moment. Customers and suppliers, debtors and creditors are structures which inform about the funds inputs and outputs. As such monetary flows can be valued; the accrual accounting is based on the funds movement. Knowing that the operations which affect the treasury are presented especially at the generation moment rather than in the payment and receipt moment, certain monetary flows forecasts could be exactly established.

It must be emphasized that „accruals” is not a „magic bullet” for improving the performance of the public sector. It is simply a tool for getting better information about the true cost of public sector institutions. It needs to be used effectively

and in tandem with a number of other management reforms in order to achieve the desired improvement in decision-making in the public sector. The application of the accounting rules is a complex strategic and political process in which every part is important.

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